

TENNESSEE GENERAL ASSEMBLY
FISCAL REVIEW COMMITTEE



FISCAL NOTE

SB 1011 - HB 995

February 28, 2013

SUMMARY OF BILL: Phases out the Hall Income Tax (HIT) over a three-year period consisting of a tax rate reduction from six percent to four percent for tax year 2014, a tax rate reduction from four percent to two percent for tax year 2015, and a tax rate reduction from two percent to zero for tax year 2016 and all subsequent years.

ESTIMATED FISCAL IMPACT:

**Decrease State Revenue – Net Impact – \$39,431,500/FY14-15
\$78,863,100/FY15-16
\$118,294,600/FY16-17 and Subsequent Years**

State Expenditures – Cost Avoidance – \$354,600/FY16-17 and Subsequent Years

**Decrease Local Revenue – Net Impact – \$24,090,700/FY14-15
\$48,181,400/FY15-16
\$72,272,100/FY16-17 and Subsequent Years**

Other Fiscal Impact – Secondary economic impacts may occur as a result of this bill. Such impacts may be realized due to changes in population or as a result of other behavioral changes prompted by the passage of this bill. Due to multiple unknown factors, fiscal impacts directly attributable to such secondary economic impacts cannot be quantified with reasonable certainty.

Assumptions:

- Pursuant to Tenn. Code Ann. § 67-2-102, HIT is a six percent tax on income derived from dividends on stock or from interest on bonds.
- Given the tax changes in this bill shall be applied to tax years beginning with tax year 2014, and assuming that 100 percent of HIT owed for tax year 2014 is collected no later than June 30, 2015, the first year impacted by this bill will be FY14-15. This collection pattern is assumed to remain constant into perpetuity.
- The current Fiscal Review Committee estimate for HIT collections in FY13-14 is \$200,070,000.
- Taxable income in FY13-14 is estimated to be \$3,334,500,000 (\$200,070,000 / 6.0%). This number is assumed to remain constant in subsequent years.

- The decrease in HIT collections is estimated to be \$66,690,000 (\$3,334,500,000 taxable income x 2.0% rate reduction) in FY14-15; \$133,380,000 (\$3,334,500,000 taxable income x 4.0% rate reduction) in FY15-16; and \$200,070,000 (\$3,334,500,000 taxable income x 6.0% rate reduction) in FY16-17 and subsequent years.
- Pursuant to Tenn. Code Ann. § 67-2-119(a), the state retains 62.5 percent of HIT revenue; local governments are apportioned 37.5 percent.

Assumptions related to FY14-15:

- The decrease in HIT revenue in FY14-15 for the state is estimated to be \$41,681,250 (\$66,690,000 x 62.5%); the decrease in HIT revenue in FY14-15 for local government is estimated to be \$25,008,750 (\$66,690,000 x 37.5%).
- Fifty percent of tax savings will be spent in the economy on other sales-taxable goods and services.
- The current state sales tax rate is 7.0 percent; the average local option sales tax rate is estimated to be 2.5 percent.
- The increase in state sales tax revenue in FY14-15 is estimated to be \$2,334,150 (\$66,690,000 x 50.0% x 7.0%); the increase in local option sales tax revenue is estimated to be \$833,625 (\$66,690,000 x 50.0% x 2.5%).
- Pursuant to Tenn. Code Ann. § 67-6-103(a)(3)(A), local governments receive 4.603 percent of state sales tax revenue as state-shared sales tax revenue.
- Pursuant to Tenn. Code Ann. § 67-6-103(q), no portion of revenue derived from the 0.5 percent sales tax rate increase, from 5.5 percent to 6.0 percent (effective April 1, 1992), or the 1.0 percent sales tax rate increase, from 6.0 percent to 7.0 percent (effective July 15, 2002), shall be distributed to local government.
- The effective rate of apportionment to local government pursuant to the state-shared allocation is estimated to be 3.617% [(5.5%/7.0%) x 4.603%].
- The increase in local revenue pursuant to the state-shared allocation in FY14-15 is estimated to be \$84,426 (\$2,334,150 x 3.617%).
- The net increase in state sales tax revenue in FY14-15 is estimated to be \$2,249,724 (\$2,334,150 - \$84,426).
- The net increase in local sales tax revenue in FY14-15 is estimated to be \$918,051 (\$833,625 + \$84,426).
- The total decrease in state revenue in FY14-15 as a result of this bill is estimated to be \$39,431,526 (\$41,681,250 – \$2,249,724).
- The total decrease in local revenue in FY14-15 as a result of this bill is estimated to be \$24,090,699 (\$25,008,750 - \$918,051).

Assumptions related to FY15-16:

- The decrease in HIT revenue in FY15-16 for the state is estimated to be \$83,362,500 (\$133,380,000 x 62.5%); the decrease in HIT revenue in FY14-15 for local government is estimated to be \$50,017,500 (\$133,380,000 x 37.5%).

- The increase in state sales tax revenue in FY15-16 is estimated to be \$4,668,300 ($\$133,380,000 \times 50.0\% \times 7.0\%$); the increase in local option sales tax revenue is estimated to be \$1,667,250 ($\$133,380,000 \times 50.0\% \times 2.5\%$).
- The increase in local revenue pursuant to the state-shared allocation in FY15-16 is estimated to be \$168,852 ($\$4,668,300 \times 3.617\%$).
- The net increase in state sales tax revenue in FY15-16 is estimated to be \$4,499,448 ($\$4,668,300 - \$168,852$).
- The net increase in local sales tax revenue in FY15-16 is estimated to be \$1,836,102 ($\$1,667,250 + \$168,852$).
- The total decrease in state revenue in FY15-16 as a result of this bill is estimated to be \$78,863,052 ($\$83,362,500 - \$4,499,448$).
- The total decrease in local revenue in FY15-16 as a result of this bill is estimated to be \$48,181,398 ($\$50,017,500 - \$1,836,102$).

Assumptions related to FY16-17 and Subsequent Years:

- The decrease in HIT revenue in FY16-17 and subsequent years for the state is estimated to be \$125,043,750 ($\$200,070,000 \times 62.5\%$); the decrease in HIT revenue in FY16-17 and subsequent years for the local government is estimated to be \$75,026,250 ($\$200,070,000 \times 37.5\%$).
- The increase in state sales tax revenue in FY16-17 and subsequent years is estimated to be \$7,002,450 ($\$200,070,000 \times 50.0\% \times 7.0\%$); the increase in local option sales tax revenue is estimated to be \$2,500,875 ($\$200,070,000 \times 50.0\% \times 2.5\%$).
- The increase in local revenue pursuant to the state-shared allocation in FY16-17 and subsequent years is estimated to be \$253,279 ($\$7,002,450 \times 3.617\%$).
- The net increase in state sales tax revenue in FY16-17 and subsequent years is estimated to be \$6,749,171 ($\$7,002,450 - \$253,279$).
- The net increase in local sales tax revenue in FY16-17 and subsequent years is estimated to be \$2,754,154 ($\$2,500,875 + \$253,279$).
- The total decrease in state revenue in FY16-17 and subsequent years as a result of this bill is estimated to be \$118,294,579 ($\$125,043,750 - \$6,749,171$).
- The total decrease in local revenue in FY16-17 and subsequent years as a result of this bill is estimated to be \$72,272,096 ($\$75,026,250 - \$2,754,154$).

Assumptions related to expenditures and secondary impacts:

- According to the Department of Revenue, the Department is currently implementing new data entry software and mandatory electronic filing requirements for HIT and other taxes administered by the Department. As a result, positions in the Processing Division are being eliminated through the budget process. In FY13-14, the Department plans to eliminate 20 positions. All positions used for processing HIT returns will be eliminated under current law, by the time the HIT would be phased out under this bill.
- The Department will redeploy all six HIT auditors to other tax audit areas once HIT is phased out. The number of auditors that the Department intends to recruit will, therefore, decrease by six, resulting in a recurring cost avoidance of \$354,648 to the Department, beginning in FY16-17.

- There could be subsequent increases in state and local government revenue and expenditures due to the secondary economic impacts prompted by the passage of this bill. Increases in revenue may occur if the state's population increases as a result of a reduced tax liability. Increases in expenditures may occur if the demand for governmental programs and infrastructure increases as a result of population increases. Due to multiple unknown factors such as the extent and timing of population changes, the fiscal impacts directly attributable to such secondary economic impacts cannot be quantified with reasonable certainty.

CERTIFICATION:

The information contained herein is true and correct to the best of my knowledge.

A handwritten signature in black ink, appearing to read 'Lucian D. Geise', written in a cursive style.

Lucian D. Geise, Executive Director

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